STATE OF MICHIGAN
CIRCUIT COURT FOR THE 30TH JUDICIAL CIRCUIT
INGHAM COUNTY

LINDA A. WATTERS, COMMISSIONER,
OFFICE OF FINANCIAL AND INSURANCE SERVICES
FOR THE STATE OF MICHIGAN,

Petitioner,

v

File No. 03-1127-CR

THE WELLNESS PLAN,
a Michigan health maintenance organization

Hon. William E. Collette

Respondent.
_____/

E. John Blanchard (P28881)
Michael J. Fraleigh (P36615)
David W. Silver (P24781)
William A. Chenoweth (P27622)
Attorneys for Petitioner, Commissioner of
the Office of Financial & Insurance Services
Michigan Department of Attorney General
Insurance & Banking Division
P.O. Box 30754
Lansing, Michigan 48909
(517) 373-1160

REHABILITATOR'S RESPONSE TO THE OBJECTIONS TO THE PETITION FOR APPROVAL OF THE REHABILITATOR'S PLAN TO SELL ASSETS OF THE WELLNESS PLAN TO AMERIGROUP MICHIGAN, INC.

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I. **The ultimate viability of the Wellness Plan depends upon the revenue from its Medicaid business. Because the Wellness Plan does not qualify to receive a new Medicaid contract, it cannot continue to operate as an HMO after September 30, 2004. Therefore, the proposed sale of assets is necessary in order to obtain the maximum benefit from the HMO's assets for the members, creditors, and the public generally.**

From the time that The Wellness Plan (TWP) was first placed into rehabilitation, the Rehabilitator sought to hold the provider network intact and implement changes that would allow TWP to operate profitably as an HMO. The goal was to continue to provide service to the members and to generate revenue to pay off the claims of creditors. That approach depended upon TWP's ability to continue to operate as a Medicaid HMO under contract with the Department of Community Health (DCH). According to TWP's annual statement for calendar year 2003, TWP's total premium for 2003 was $228,913,367. Of that amount, $208,923,808 came from the Medicaid business. In other words, fully 91% of TWP's premium income derived from its Medicaid business. The Medicaid business was clearly essential to the prospects for successful operation of TWP as a going concern.

Those prospects disintegrated when the DCH decided to rebid the Medicaid contracts. In order to receive a Medicaid contract under the DCH Invitation to Bid, a bidder must meet all applicable statutory financial requirements set forth in the Michigan Insurance Code. Invitation to Bid, Section IV-B, p 76. TWP fails to satisfy at least two critical statutory financial requirements. First, TWP has reported to the Office of Financial and Insurance Services on Form FIS 321 (December 31, 2003) that it has a ***negative working capital reserve of $29.4 million***. Therefore TWP is not in compliance with section 3555(b) of the Insurance Code, which requires that an HMO have adequate working capital "which shall not be negative at any time." MCL 500.3555(b). This alone is sufficient to disqualify TWP from receiving a new Medicaid contract under the DCH invitation to bid.

But negative working capital is not the only reason TWP does not qualify for a new Medicaid contract. Section 403 of the Insurance Code requires that an HMO must be "safe, reliable, and entitled to public confidence" as a condition precedent to maintaining its authority to do business in Michigan. MCL 500.403. Section 3551(4) of the Code requires that the OFIS Commissioner consider Risk Based Capital (RBC) requirements, as developed by the National Association of Insurance Commissioners, when determining if an HMO is "safe, reliable, and entitled to public confidence" under MCL 500.403. RBC requirements are described in Insurance Bureau Bulletin 98-02. The established standard, to measure minimum needed capital given the health plan's size and risk profile is 200% RBC. The Wellness Plan is at 122% RBC, which is $5.5 million short of 200% RBC level.[1] For this independently sufficient reason, TWP does not qualify for a new Medicaid contract to take effect when its current contract expires on September 30, 2004.

As a consequence, the overriding issue for the Rehabilitator is how to capitalize to the maximum extent possible on the assets available to TWP. Although TWP does not qualify for a contract, it has members and a certificate of authority that are very valuable ***for a limited period of time***. TWP's membership and certificate of authority are valuable to Amerigroup because they will put Amerigroup in a position to bid for a Medicaid contract which they would not otherwise be in a position to bid for. But the value of this asset to TWP and its creditors is fleeting. ***After May 14, 2004, the deadline for submission of bids to DCH, the value evaporates***. If TWP does not make the sale as proposed and the deadline passes, then DCH will simply reassign TWP's Medicaid members to another HMO ***and TWP and its creditors will receive no value in return***. This is, therefore, undeniably a case where time is of the essence to

[1] Affidavit of Judith A. Weaver, paragraph 5, attached hereto as Attachment 1.

protect the interests of creditors, who are predominantly health care providers, by capitalizing on this fleeting asset.

It appears inevitable that there will eventually be a liquidation of TWP after its Medicaid contract expires on September 30, 2004. If this sale is approved and on May 14, 2004 Amerigroup successfully bids for a Medicaid contract with DCH, we can expect approximately $38 million from the sale to go toward satisfying the liabilities of the creditors, the members will have continuity of service to the extent that the provide network can be preserved, and there could possibly be excess assets dedicated to a charitable purpose. If this sale is not approved before May 14, then there will be no proceeds to fund payments to creditors, the membership can be expected to lose continuity of care when DCH assigns them to a new HMO, and there will surely be no excess assets available for any charitable endeavor. Clearly, there is much at stake at this juncture and the Rehabilitator's decision to accept the bid from Amerigroup is a sound exercise of her discretion to protect the interests of the members, the creditors, and the public in general under the realities she faces. The Court should approve the Rehabilitator's decision and allow the sale to go forward without delay.

II. The Rehabilitator's best and final offer process for eliciting bids was necessary, fair, and within the Rehabilitator's discretion.

A. The Rehabilitator has great discretion in dealing with the property and business of the insurer.

There is no statutory procedure proscribed in Chapter 81 for eliciting bids for the purchase of HMO assets. The Commissioner, however, is given great discretion and is statutorily empowered to "reform," "revitalize," "transform," "convert," and to "deal with the property and business of the insurer." MCL 500.8114. The Commissioner, as Rehabilitator, has this wide-reaching authority and is ***vested by operation of law with title to ALL the assets of the insurer***. MCL 500.8113. A time consuming public notice process for accepting offers, as

suggested by some of the objectors, is not required by Chapter 81. In fact, public notice could very well have created unwarranted concern and fear for the members and creditors causing instability in the network and jeopardizing the most vital asset of the HMO; its membership. Without question, knowledge of a potential asset sale would have created turmoil within the healthcare community in southeastern Michigan. The Commissioner, as Rehabilitator and chief officer of the Michigan Office of Financial and Insurance Services, is the regulator of HMOs, insurance companies, and other insurance related entities. As the Michigan regulator, the Rehabilitator is uniquely qualified to assess the financial viability of potential bidders. Public notice potentially would have brought parties into the process that did not have the financial wherewithal or expertise to run a successful health plan. Given the time constraints imposed by the DCH Medicaid bidding process, and the recognition that TWP could not secure a new Medicaid contract due to its financial prerequisites imposed by the Department of Community Health, the Rehabilitator exercised her discretion and acted prudently to maximize the receivership assets for the benefit of creditors. The level of capital needed to consummate these purchases is very high and the level of expertise needed to successfully run health plans with the membership from these health plans is extensive. Very few parties could meet both of these criteria. All interested parties that contacted the Rehabilitator or OFIS were given equal opportunity to sign confidentiality agreements until the first week in March 2004, and to submit offers until March 17, 2004. Potential buyers have approached the Rehabilitator since July 2003 about purchasing the health plan. The rehabilitation of TWP has certainly been no secret. Anyone could have submitted an unsolicited written offer since TWP was placed in Rehabilitation in July of 2003 or since MDCH announced its intention to rebid its Medicaid contract. The rehabilitations and Medicaid contract were discussed in the local media. Out-of-

state firms heard about the rehabilitations and rebid of MDCH's Medicaid contract. Any firms, including local firms could have pursued the opportunity. Best and Final Offer letters were sent March 9 to all interested parties that had signed confidentiality agreements and continued to be actively engaged in discussions with the Rehabilitator regarding potential purchase of the health plans. The Best and Final Offer process gave interested parties equal opportunity to submit their best offers to the Rehabilitator for final consideration before any exclusive relationships were entertained by the Rehabilitator. The Best and Final offer process allowed the Rehabilitator to make informed decisions and move forward with selected buyers. The reality presented is that there simply is not sufficient time between now and when the MDCH proposals are due to entertain offers from any new interested parties. If no sale is consummated, the membership will be redistributed to other health plans ***without compensation*** to TWP.

B. **The Rehabilitator's best and final bid letter was necessary and appropriate.**

Faced with the eventual reassignment of its 103,000 members to other health maintenance organizations without compensation to the receivership estate, and to preserve the maximum value for the creditors, the Rehabilitator determined that it was necessary, and in the best interests of the members, creditors, providers, and the public to solicit offers from interested parties for the sale of TWP to another entity that would be eligible to bid on the Medicaid contract. A Request for Bid letter on behalf of the Rehabilitator was issued on March 9, 2004, soliciting offers from interested buyers to submit their best and final offer to the Rehabilitator for the purchase of assets of TWP. A representative copy of the Request for Bid letter is attached to the Rehabilitator's Petition at Tab 1.

The Request for Bid letter set forth a timeline for the bid process, and enumerated criteria that the Rehabilitator would consider when making her best judgment to determine which offer or combination of offers would best meet the needs of the creditors, members, and the public as a

whole. The bid letter also stated unequivocally that all decisions on the bids were subject to the sole discretion of the Rehabilitator and would require the approval of the rehabilitation court. Section C of the Request for Bid Letter, attached to the Rehabilitator's petition as Tab 1, provided as follows:

> The rehabilitator will use her ***best judgment*** to determine which bid or combination of bids best meet the needs of the HMOs' creditors, members and the public as a whole. ***All decisions will be subject to the sole discretion of the Rehabilitator and will require approval by the rehabilitation court***....
> (Emphasis added)

The factors that were given careful consideration by the Rehabilitator in evaluating the proposed bids included:

a. Are the bids fair and equitable to the creditors, members and the public as a whole?
b. Will the bids provide full payment to the creditors?
c. How are post rehabilitation liabilities treated?
c. What assets are being acquired?
e. Commitment to employ current staff.
f. How much is being paid?
g. Operational experience and history of the bidder and its management, including regulatory history.
h. Availability of funds to complete the transaction and any contingencies related to the availability of funds.
i. Financial reserves and solvency of the bidder and the proposed new entity, if any.

The process utilized allowed the entities and individuals who had expressed an interest in purchasing one or both of the health care plans to provide their best and final offer. This request for best and final offer was made after the individuals and entities had an opportunity to perform due diligence, review the financial records of the company, review the provider contracts, and review the operations of the entities.

C. Confidentiality agreements were executed between all bidders and the Rehabilitator

In order to enable the interested parties to perform the necessary due diligence, it was mutually understood and agreed that Confidentiality Agreements between all prospective bidders and the Rehabilitator would be required. The Confidentiality Agreements required the protection of non-public confidential or information proprietary in nature. It included such documents as analyses, compilations, forecasts, studies, goals and objectives, business and developmental and strategic plans, or other documents which contained or reflected confidential information. The confidentiality agreements obligated the parties to keep confidential and not disclose in any manner, without prior written consent, any confidential material, including any bid submissions. The degree to which each of the individual entities took advantage of their opportunity to conduct due diligence under the confidentiality agreement varied from entity to entity. The process did not lock any of the potential bidders into a set formula or framework for their offer. To the contrary, all were free to use their business judgment and creativity to craft the best deal possible for the health plan and the receivership estate. Accordingly, anyone who had expressed an interest in purchasing the health care plans was provided an opportunity to bid. The process was opened to asking for best and final bids from all individuals who had expressed sufficient interest in the health care plans to enter into confidentiality agreements and conduct due diligence investigations. Bidders who had made inquiries but had not pursued discussions regarding the purchase of one or more of the health plans, or entered into a confidentiality agreement or otherwise indicated that they were interested and willing to go forward in the evaluation process were not sent requests for bids. All bid discussions with the potential bidders were done on a non-exclusive basis, which was known to all the individuals and entities with whom the matter was discussed.

On March 17, 2004, the Rehabilitator received offers from four interested parties for the purchase of the assets of TWP. The bidders were interested in purchasing TWP's Medicaid members, provider network, license to operate a health maintenance organization in Michigan and other miscellaneous assets. The Rehabilitator carefully reviewed the merits of each of the four proposed offers to determine which offer was in the best interest of TWP, its members, the creditors, the providers, and the public, and which offer best satisfied the criteria set forth in the Request for Bid issued by the MDCH.

D. **Amerigroup best satisfied the selection criteria and interests involved, and was within the Rehabilitator's discretion**

The Rehabilitator analyzed the offers received on March 17 from the interested buyers of TWP. Offers were received from Amerigroup Corporation, Molina HealthCare, Inc., Ion Health, Inc., and another entity, which has not objected. The Rehabilitator determined that the offer from Amerigroup, a Michigan corporation, best satisfied the selection criteria and the interests of TWP, its members, the creditors, including the providers, and the public. Amerigroup offered to purchase TWP's contract to serve the members, the health maintenance organization's certificate of authority and provider contracts for $38 million. The Rehabilitator determined that the offer from Amerigroup would:

a. maximize the amount of return to the creditors of TWP.

b. provide continuity of care to the 103,000 members of TWP.

c. provide that the provider agreements remain in effect on the same terms and conditions for a minimum of 12 months following the closing.

d. provide the opportunity for continued employment to some of the current TWP.

The Rehabilitator's sale of TWP's assets to Amerigroup under the terms and conditions set forth in the Letter of Intent is fair and equitable and in the best interest of the creditors, providers, and members of TWP and the public as a whole. These terms include:

1. Amerigroup will pay $38,000,000.00 in cash for the Medicaid business. The purchase price will be decreased by $368.93 per member to the extent the actual transferred membership is less than 103,000 members 30 days following the effective date of the transfer.

2. Amerigroup would acquire the HMO license.

3. Amerigroup will be in compliance with all HMO financial requirements by closing.

4. TWP's Medicaid Provider Agreements will remain in full force and effect until the later of September 30, 2005 or the termination date in the specific Medicaid Provider Agreement.

5. The Assets, as defined in the Letter of Intent, will be transferred or assigned to Amerigroup free and clear of all claims, liens, encumbrances, obligations, liabilities or other interests, including, without limitation, Excluded Claims as defined in the Letter of Intent. All liabilities and obligations that accrue before October 1, 2004 shall remain with TWP and shall be paid, discharged or otherwise resolved as part of this Court's receivership proceedings, and Amerigroup shall have no liability of any kind for such liabilities and obligations. The Court will retain exclusive jurisdiction to resolve any liabilities or obligations that are asserted against Amerigroup after the Closing.

6. Amerigroup commits to being in compliance in all material respects with all applicable laws, rules and regulations.

7. The parties shall have received all applicable governmental authorizations, consents and approvals, including, without limitation, approvals of the Centers for Medicare & Medicaid (CMS), Michigan Department of Community Health, Michigan Office of Financial and Insurance Services, and the Rehabilitator as applicable.

E. **Analysis of other offers**

The second best offer was Molina HealthCare in terms of (1) dollars into the estate, and (2) financial wherewithal of the buyer (copy of Molina offer attached to Molina objections filed with Court). Its offer of $38 million was to purchase the contract to serve the TWP membership **and** the seven properties currently owned by TWP. However, TWP has the properties valued on its December 31, 2003 financial statements at $20,275,152. The recently appraised fair market value of five of the properties is $25.8 million. Assuming the properties are worth the $20.3 million, Molina offered only $17.7 million for the contract to serve the members. Amerigroup is offering $38 million for the membership which does **not** include the properties. Therefore, the Rehabilitator determined that Amerigroup's purchase offer was higher and more advantageous than Molina's because the receivership estate will still own the properties that can be sold for additional monies which will become part of the receivership estate for the distribution to TWP creditors. According to the 10-k filed with Molina's offer, Molina had cash and cash equivalents of $142 million as of December 31, 2003. This is $393 million less than Amerigroup. Further, given Molina's already staffed operations in Michigan, the rehabilitator also believed that fewer jobs would be offered to TWP's currents employees.

The major concern of the rehabilitator with the Ion offer is that funds necessary to complete this transaction do not currently exist (copy of Ion bid attached to Ion objections filed with Court). Ion has stated that it has engaged the financial services of Merrill Lynch to raise the capital necessary on Wall Street to complete this transaction and ultimately run a financially secure health plan. Ion has not adequately demonstrated to the Rehabilitator that the cash is readily available. In order to raise the capital, investors would most likely require Ion to demonstrate it was awarded a new Medicaid contract. Given the requirements in the Invitation to Bid, the Rehabilitator had concerns that Ion would not be successful in being awarded a

contract without the funds readily available. Definitely, the transaction could not be consummated unless Ion was successful in raising the funds. If Ion fails to raise the funds, MDCH would terminate any contract it might have awarded to Ion and move the members to other HMOs without compensation to TWP or its creditors. Ultimately, the TWP creditors might not be paid.

On the other hand, the selected buyer, Amerigroup, has the cash readily available. Ion's offer indicates a per member price of **$305.00** versus the selected buyers purchase price of **$368.93**. Amerigroup's offer provides more value to the creditors of TWP. Ion's objection discusses its combined offer. However, the Rehabilitator has a fiduciary responsibility to marshal the assets of this TWP receivership estate so as to maximize the value to TWP creditors. Amerigroup's offer does that by offering $368.93 per member as opposed to Ion's $305.00 per member.

Further, Ion has no demonstrated track record in running a successful health plan. According to Ion's financial statement ending December 31, 2003 submitted to the Rehabilitator with its bid, Ion commenced business as recently as this month, April 1, 2004. Ion has no premium reported because it did not start its operations as of the filing of the financial statements. Ion has disclosed to the Rehabilitator a license for only one health plan in Pennsylvania. It is believed that its first enrollment of members also occurred just this month, April of 2004. According to Ion, the management team has experience with other health plans. However, this experience is not in operating together as the management team of Ion, the bidder.

Amerigroup, on the other hand, is a multi-state managed health care company focused exclusively on providing health care services for low-income families, the disabled, and the

uninsured within the Medicaid programs. Amerigroup is a publicly traded stock corporation headquartered in Virginia Beach, Virginia. Amerigroup has demonstrated its ability to successfully provide managed health care for more than 857,000 members in six states. At the end of 2003, Amerigroup had cash and investments that totaled $535 million, with available cash more than adequate to complete the transaction. Ion has no such proven track record. Ion reports as of December 31, 2003, $8.2 million in cash and investments as compared to Amerigroup's $535 million.

Further, the Ion offer indicates that only $24.6 million would be available for the pre-rehabilitation claims of TWP and OmniCare surplus notes, and $3.1 million for charitable distributions from the plans. This totals $27.7 million. Ion has indicated that $16.5 million would be invested to bring the plans into compliance with equity and working capital requirements, $3.7 million to assure sufficient working capital to Ion, $2.3 million for system implementation and conversion costs, and $5.0 million for malpractice contingencies. Thus, the remaining portion of the $55.2 million that is not part of the $27.7 will remain under the exclusive control of the new Ion company and be paid under the company's timing and discretion. The $38 million cash paid by Amerigroup, on the other hand, will become part of the receivership estate under the supervision of the rehabilitator and the court to be distributed pursuant to the statutory scheme set forth for liquidation in chapter 81 of the Insurance Code. Ion's $24.6 million most likely would not result in full payment to all. Ion would then be responsible for paying the other creditor's liabilities (post-rehab) of both health plans. Therefore, there is a certain credit risk to the creditors with Ion's offer that does not exist in Amerigroup's offer.

Finally, as part of the best and final offer process, the buyers provided the Rehabilitator background information such as financial statements and biographical information. In reviewing this information, the Rehabilitator found a disclosure that was very troubling. The disclosure was of a nature that could prevent the approval of the change of control (i.e. purchase of the health plans) to Ion by the Commissioner of the Office of Financial and Insurance Services. The Amerigroup information did not result in similar concerns.

The final offer of another entity was well below all other offers and was therefore unacceptable.

The Rehabilitator's proposal to sell assets of TWP to Amerigroup has been designed to provide the greatest relief possible to the creditors of TWP while protecting the interests of its members and the public. Amerigroup and has a proven track records to run successful health maintenance organizations. It has multiple health maintenance organizations in multiple states. It is a publicly traded entity so they also have access to additional capital. Amerigroup has capital and surplus of $462 million and cash and investments of $535 million. Amerigroup has the financial resources to complete the purchase of one or both plans.

III. The objections of the losing bidders, Molina and Ion should be disregarded because for more than a century Michigan law has clearly provided that losing bidders have no standing to challenge the bid process

State law is clear that a losing bidder on a public contract lacks standing and is precluded from judicially challenging the bid process and the decisions made with respect to it. Michigan law vests no rights in bidders or potential bidders on State contracts due to their lack of standing. Federal court decisions have reaffirmed this aspect of Michigan law. This is because a losing bidder is not within the class of persons intended to be benefited by the competitive bidding process for state contracts.

This long-established rule applies with even greater force in the context of this rehabilitation procedure under Chapter 81 of the Insurance Code. Clearly the focus of the Rehabilitator's obligation under Chapter 81 is to protect the interests of the members and creditors of the receivership estate and the public generally. It is ***not*** to protect the interests of losing bidders like Molina and Ion. Just as losing bidders in a public contact case are not within the class of persons intended to be benefited by laws requiring public bidding, losing bidders in this rehabilitation proceeding are not within the class of persons intended to be protected in the rehabilitation. Furthermore, unlike the public contract cases, where statutory provisions frequently mandate a competitive bid process, there is no analogous statute requiring that the Rehabilitator base her decision on a competitive bid process or that she accept the highest bid. The Rehabilitator simply chose this bid process to protect the interests of the rehabilitation members, creditors, and the public. Moreover, the invitations to bid sent out on the Rehabilitator's behalf in this case clearly provided that: "All decisions will be subject to the sole discretion of the Rehabilitator . . ." subject to approval by this Court. Hence bidders were put on notice from the outset that the decision to accept or reject any offer was discretionary with the Rehabilitator. It follows that the objections filed by the losing bidders, Ion and Molina, must be disregarded because they lack standing.

More than a century ago, the Michigan Supreme Court recognized the rule precluding a bidder from challenging a public agency's contracting decisions in *Talbot Paving Co v Detroit*, 109 Mich 657; 67 NW 979 (1896). In *Talbot*, the Court ruled that the plaintiff, a losing bidder, lacked standing to challenge the bid process because the City's competitive bid statute was designed to protect and benefit the public, rather than the private interests of a bidder:

> While, under the charter of Detroit, it was the duty of the city to let the contract to the lowest responsible bidder, yet this charter provision was not passed for the

benefit of the bidder, but as a protection to the public. We think the rule as stated in Strong v Campbell, 11 Barb 138, is the true one, and the one which has always been adhered to by the courts. It is there stated as follows:

> Wherever an action is brought for a breach of duty imposed by statute, the party bringing it must show that he had an interest in the performance of the duty, and that the duty was imposed for his benefit. But where the duty was created or imposed for the benefit of another, and the advantage to be derived to the party prosecuting, by its performance, is merely incidental, and no part of the design of the statute, no such right is created as forms the subject of an action. [*Talbot, supra* at 660-661 (emphasis added).]

The century-old principles in *Talbot* apply today and with equal force to the objections of the losing bidders in this rehabilitation. The Rehabilitator's invitation to bid was not intended for the protection of the bidders. It was intended to protect the interest of "the creditors, members and the public as a whole." As the Court in *Talbot Paving* explained, because the competitive bidding process is designed to benefit the public, not the bidders, a losing bidder has no standing to object.

This principle of standing was affirmed in *Detroit v Wayne Co Judge*, 128 Mich 438, 439; 87 NW 376 (1901), when the Supreme Court, called upon to review the grant of a preliminary injunction to a disappointed bidder, summarily ruled that as a bidder, complainant has no standing. The Court dismissed the lawsuit, holding that a bidder has no right to maintain an equitable action to set aside a governing body's award of a public contract.

Malan Construction Corp v Wayne Co Bd of Rd Comm'rs, 187 F Supp 937, 939 (ED Mich, 1960), reaffirmed the principle that the benefit of competitive bidding runs directly to the community, rather than to the bidder:

> Competitive bidding is not intended to benefit bidders. It is designed to protect the tax-paying public from fraud or favoritism in the expenditure of government funds. . . . The Michigan Supreme Court has held that the duty of public officials to consider honestly competitive bids runs directly to the community and that, therefore, only the public, through the taxpayer's suit, has standing to enjoin a

> proposed contract. **The incidental benefit received by bidders from competitive bidding does not allow an unsuccessful bidder to bring a private action.** [Emphasis added.]

The Court expressly rejected the plaintiff's argument that *Talbot* only precluded losing bidders from seeking damages, but allowed them to seek injunctive relief. 187 F Supp at 939.

Similarly, in *City Communications, Inc v City of Detroit*, 650 F Supp 1570 (ED Mich, 1987), the plaintiff, a bidder for the City of Detroit's cable television franchise, brought an action challenging the bidding process. Despite the allegations of fraud, conspiracy, and collusion in the bid process, the court dismissed the claims finding:

> **[T]he law of Michigan gives no rights to unsuccessful bidders . . . ,**
>
> [D]isappointed bidders have no standing to challenge the award of public contracts . . . not even claims of fraud or conspiracy have been held to give unsuccessful bidders a cause of action, because honest and competitive bidding is not intended to protect the bidders, but rather is designed to protect the taxpayers from fraudulent and dishonest expenditures. **Michigan courts, therefore, hold that only the public, and not the bidder, has standing to challenge the bidding process.** [*Id.* at 1581 (emphasis added).]

In *Long Mechanical, Inc v River Rouge School District*, 1997 Mich App LEXIS 1506 (1997) the Court of Appeals confirmed that losing bidders have no standing to challenge the bid process even where they assert "fraud, injustice or illegality."

> We agree with the decision in *Great Lakes* [*Heating and Cooling, Refrigeration & Sheet Metal Corp*, 197 Mich App 312; 494 NW2d 863 (1992)] insofar as it states that we will not interfere with public bids unless there is fraud, injustice or illegality. See Berghage v City of Grand Rapids, 261 Mich 176; 246 NW 55 (1933); Leavy v City of Jackson, 247 Mich 447; 226 NW 214 (1929). However, ***we find that only taxpayers have standing to bring the cause of action and allege fraud, injustice or illegality***. In both Berghage and Leavy, taxpayers brought suit to enjoin the defendant municipalities from awarding contracts to the higher bidders. Had the issue of standing been raised in *Great Lakes*, we are confident that the Court would have found no standing for the disappointed bidders, following Michigan precedent. [emphasis added.]

In *United of Omaha Life Ins Co v Solomon*, 960 F2d 31, 34 (CA 6, 1992), the court found no cause of action by a disappointed bidder on a state contract for administrative services relative to a life insurance program:

> Michigan statutory and case law neither requires that the lowest bidder be awarded a state contract nor creates a property interest in disappointed bidders on state contracts. [Emphasis added.]

In *Attorney General, ex rel Allis Chalmers Co v Public Lighting Comm of City of Detroit*, 155 Mich 207; 118 NW 934 (1908), the public, represented by the Attorney General, moved to restrain the Detroit Lighting Commission from entering into a contract for the installation of an electrical generating plant. The Supreme Court explained that an action such as this, on behalf of the public, was the only proper avenue for review of a governing body's decision regarding the award of a contract:

> The proceeding is the proper one to determine the question, and the only one by which any action could be taken. The public represented by the proper officer is the real complainant before the court. [*Id.* at 211. *See also Rayford v Detroit*, 132 Mich App 248, 256; 347 NW2d 210 (1984) (referencing the "disappointed bidder" rule).]

There are strong public policy reasons for prohibiting losing bidders from initiating judicial challenges to the bid process. The economic self-interest of a bidder is secondary to the interests of the creditors, members, and the public. If losing bidders such as Ion and Molina are permitted to object, they may harm the interests of the creditors, members and the public by tying up the process for significant periods of time and causing the Rehabilitator to incur additional administrative and legal expenses, all of which must be paid from the assets of the receivership estate. This is no mere conjecture. Indeed, Ion's objection proposes a complicated and involved discovery process of all the documents, many of them provided to the Rehabilitator under confidentiality agreements, involved in the bidding process followed by a review

procedure supported by no legal authority whatever. Ion's approach would force the Rehabilitator to negotiate Asset Purchase Agreements with ***both*** Amerigroup and Ion simultaneously and would have the Court approve ***both*** agreements so that there would be two applications to DCH for Medicaid contracts.[2] This procedure is not only unsupported by any citation of authority, it would double the work required by the Rehabilitator, the Deputy Rehabilitators, and their legal counsel. Moreover, it would completely undermine the integrity of the Rehabilitator's invitation to bid process, which contemplated selecting one winning bidder and making one bid to the DCH. The next time that the Commissioner as Rehabilitator seeks a buyer for a troubled HMO, her credibility will be severely compromised. Potential bidders may well be unwilling to bid if the bidding process is subject to complete rejection and overhaul by the Court at the demand of a losing bidder.

IV. The Rehabilitator's invitation to bid on the TWP assets expressly provided that "[a]ll decisions will be subject to the sole discretion of the Rehabilitator and will require approval by the rehabilitation court." The Rehabilitator exercised her discretion in accepting the bid of Amerigroup and the Court should not reject that decision absent allegations that the decision was "arbitrary, unjust, or in bad faith"

Clearly, the losing bidders, Ion and Molina, have no standing to challenge the bid process or the Rehabilitator's decision to select Amerigroup's bid. As demonstrated in the immediately preceding section of this brief, even if the losing bidders were alleging "fraud, injustice, or illegality," they lack standing. But even where an objector has standing, unlike Ion and Molina, the case law provides that the courts will not interfere unless the decision is arbitrary, unjust, or in bad faith. There are no such allegations in this case from any party with standing to object.

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[2] Moreover, since DCH is not a party to this proceeding, it is not at all clear that it would even accept bids under these circumstances because, among other potential shortcomings, neither bidder would have a certificate of authority and neither would have an established provider network.

In *Levy v City of Jackson*, 247 Mich 447; 226 NW 214 (1929), the Court affirmed the lower court decision dismissing a challenge brought by taxpayers to city's award of a contract to publish newspaper notices. The Court quoted and applied the following rule:

> The exercise of discretion to accept or reject bids will only be controlled by the courts when necessary to prevent fraud, injustice or the violation of a trust. The court will indulge the presumption that the authorities acted in good faith in awarding the contract. [247 Mich at 450, quoting from McQuillin on Municipal Corporations (2d Ed).]

Four years later the Court cited and followed *Leavy, supra* in *Berhage v City of Grand Rapids,* 261 Mich 176; 246 NW 55 (1934). *Berhage* involved bids for publishing contracts entered into by the City of Grand Rapids. The trial court dismissed the claim that the city counsel's decision was arbitrary, unjust, and in bad faith and the Supreme Court affirmed in reliance on *Leavy*. That same year the Court cited and relied on *Leavy* again in *Robinson v. Saginaw*, 267 Mich 557, 255 NW 396 (1934) in affirming the circuit court's dismissal of a taxpayer's challenge to the award of city contracts for water meters in a competitive bidding process. The Court ruled: "we cannot find that the action of the city commission in accepting the bid of the larger newspaper was arbitrary, unjust, or in bad faith." *Id at* 451. The Court applied the same rule in *Bolt v. Board of Road Comm'rs*, 277 Mich 75, 79-80; 268 N.W. 817 (1936). More recently the Court of Appeals cited and followed *Leavy, supra* in *J.J. Zayti Trucking, Inc. v. Detroit*, 137 Mich App 705, 359 NW2d 201 (1984).

The vitality of this rule was reaffirmed in 1992 in *Great Lakes Heating, Cooling, Refrigeration & Sheet Metal Corp. v. Troy School Dist.*, 197 Mich App 312, 314; 494 NW2d 863 (1992). In that case the circuit court ordered the school district to open and consider a bid that had been delivered only 5 minutes after the 2 PM deadline specified in the invitation to bid. The

school district subsequently awarded the contract to the untimely bidder. On appeal, the Court of Appeals reversed citing *Leavy, supra* and *JJ Zayti Trucking, supra.*

> The exercise of discretion to accept or reject bids will only be controlled by the courts when necessary to prevent fraud, injustice, or the violation of a trust. The courts will indulge the presumption that the authorities acted in good faith. *J J Zayti Trucking v Detroit* , 137 Mich App 705; 359 NW2d 201 (1984), lv den 422 Mich 940 (1985), *Leavy v Jackson*, 247 Mich 447; 226 NW 214 (1929).

The Court went on to explain some of the policy reasons supporting this rule as follows:

> We recognize that judicial intervention in procurement necessarily results in delay and the expenditure of funds on behalf of all parties. We hold that a trial court cannot disturb the decision of a school board on a bid unless there has been some form of fraud, abuse, or illegality. See *Sea-land Services, Inc, v Brown* , 600 F2d 429 (3d Cir, 1979), *Bud Johnson Construction of Minnesota v Metropolitan Transit Comm*, 272 NW2d 31 (Minn, 1978) and *Nole & Son, Inc v Bd of Education of the City School District of Norwich*, 514 NYS2d 274; 129 AD2d 873 (1987). We find that to hold otherwise would create a floodgate of litigation which would benefit neither the public authority nor the citizens and taxpayers it is attempting to represent and serve.

The logic of these cases applies with equal force in this case. The Rehabilitator conducted a competitive bid process although she was not required to do so by any applicable law. The process that she followed allowed all persons who had expressed an interest in bidding on asset of TWP an equal opportunity to compete. The invitation to bid itself expressly provided that:

> The rehabilitator will use her best judgment to determine which bid or combination of bids best meet the needs of the HMOs' creditors, members and the public as a whole. All decisions will be subject to the sole discretion of the Rehabilitator and will require approval by the rehabilitation court.

As shown in the second section of this brief, the Rehabilitator conducted a careful review of the bids and exercised her discretion upon pertinent criteria. This Court ought to, as did the Courts in *Leavy, Berhage, Robinson, JJ Zayti,* and *Great Lakes* "indulge the presumption" that the Rehabilitator acted in good faith. Where, as here, the decision is discretionary and there are

no allegations, let alone proof, of fraud, injustice, or violation of trust, there is no basis for this Court to reject the Rehabilitator's decision.

Moreover, the policy concerns identified by the Court of Appeals in *Great Lakes Heating, supra* squarely apply to this case. If this Court were to consider the bids de novo, the inevitable result would be the loss of critical time and increased expenses on the part of the Rehabilitator, her Deputy Rehabilitators, and her legal counsel, all of which are expenses payable dollar for dollar from the receivership estate.

In light of the foregoing case law and the circumstances of this case in particular, the Court should deny the objections and approve the Rehabilitator's plan to sell the assets of TWP for the benefit if the members, the creditors, and the public generally. Unlike any other person before this Court, the Rehabilitator is uniquely situated to make this decision and completely without a personal financial stake in the outcome.

V. The vast majority of TWP's medical providers do not object to the assignment of their provider contracts to Amerigroup of Michigan

TWP contracts with its medical providers all require the consent of the provider to assign the contracts to Amerigroup. Notice of the proposed contract assignment was provided to all of Wellness is medical providers. TWP has hundreds of medical providers consisting of hospitals, clinics, physicians, medical equipment suppliers, and other individuals and entities that provide goods and services related to medical care and treatment of its members.

Out of hundreds of medical providers, only a few have objected to the proposed assignment to Amerigroup and the continuation of the contracts until September 30, 2005. One provider, Detroit Medical Center (DMC), did not object to the assignment of its contract to Amerigroup but did object to the terms of the assignment. DMC would like assurances that its

pre-rehabilitation and post-rehabilitation claims will be paid. In addition, DMC would like the ability to terminate its contract on 120 days notice.

Five of the providers that objected to the assignment of their provider agreements have indicated that if the Court orders the assignment and continuation of their contracts through September 30, 2005, they should receive the following assurances and protections:

1. The providers will be allowed to terminate their currently existing contracts pursuant to the terms and conditions on the contract starting on or after September 30, 2005.

2. The Rehabilitator will not seek an additional extension of their current contracts beyond September 30, 2005.

3. During the period of October 1, 2004 through September 30, 2005, Amerigroup will provide full and timely payment of all provider claims pursuant to the terms and conditions of their existing provider agreements and as required by law.

4. That the providers be allowed to terminate their contracts if Amerigroup does not make full and timely payment consistent with their applicable contract and Michigan law.

5. Priority payment of the provider claims from the sale proceeds.

The Rehabilitator and Amerigroup believe that these requests are reasonable. The Rehabilitator's proposed order approving the sale of the assets and the transfer of the provider contracts to Amerigroup includes provisions to guarantee providers all of the requested protections except one, priority payment from the sale proceeds.

VI. The proceeds from the sale of assets cannot be legally be restricted for the benefit of the medical providers

Five of TWP's providers have asked that the proceeds of the sale of the assets be restricted for the payment of the medical providers pre and post rehabilitation claims. In recognition of their sacrifice, both the Rehabilitator and Amerigroup would like to accommodate

the provider's request. Michigan law, however, does not allow the Rehabilitator or the Court to grant the providers a preferential priority payment at the expense of other creditors.

The approval of the proposed transaction will result in the transfer of TWP's license and Medicaid members to Amerigroup, effective October 1, 2004. After the transfer of the assets, the Rehabilitator will move the Court for an order of liquidation under MCL 500.8101 *et seq*. The claims payment procedures under liquidation are prescribed by MCL 500.8142, which provides:

1. Claims must be paid by the type of claim in the order prescribed by MCL 500.81 42 (1).

2. All claims of the class of claims must be paid in full before the next class of claims can be paid.

3. All claims within a class of claims must be treated the same. There can be no subclasses within a class of claims.

4. The claims classes are paid in the following order:

A. Class 1 Cost and expenses of administration.

B. Class 2 Claims under policies for losses incurred including third party claims.

C. Class 3 Claims of the federal government.

D. Class 4 Claims against the insurer for liability for bodily or injury to or destruction of tangible property that are not under policies and to the extent not included in Class 1 claims, that subdue employees for services performed within one year before the filing of a petition for liquidation.

E. Class 5 Claims under neither accessible policies for unearned premium or other premium refunds and claims of general creditors.

F. Class 6 Claims of state and local governments.

G. Class 7 Claims filed late or any other claim not included in Class 8 or 9.

H. Class 8 Surplus notes and similar obligations.

I. Class 9 Claims of shareholders or other owners.

Under MCL 500.8142, the providers are general creditors of TWP with Class 5 claims. MCL 500.8142(1)(e). The liquidator, Commissioner Watters, cannot make a separate subclass of claims for the providers that would give them priority over the other general creditors. MCL 500.8142(1). The liquidator is required to pay in full the claims in Classes 1-4 before any money can be paid to the Class 5 claims. *Id.* Furthermore, all Class 5 claims must be paid either in full or on a pro rata basis if they're not sufficient funds to pay the claims in full. *Id.*

The Court may also note that any payment made to the providers prior to TWP being placed into liquidation would be a preferential payment that the liquidator would be required to recover for the benefit of all creditors. MCL 500.8128.

VII. The sale of the assets is expected to generate sufficient funds to fully pay the Medical providers' claims

The providers are understandably concerned about how they benefit from the sale of the assets and the assignment and continuation of the contracts. The following analysis, will not a guarantee of payment, will give the providers an indication of how they will benefit from the proposed transaction.

The Deputy Rehabilitator indicates that total outstanding pre-rehabilitation non-medical provider claims total $1,310,094. This amount includes $426,920 of claims for which timely proof of claims have not been filed. Total medical provider claims are $24,570,540. This includes $5,031,875 of medical provider claims for which a timely proof of claim was not filed. Accordingly, based on the Rehabilitator's calculations, TWP's **total** outstanding liability for pre-rehabilitation claims is $25,880,634. The proposed sale of TWP's Medicaid membership and

HMO license will generate approximately $38 million in revenues. This leaves a net balance of approximately $12 million.

The Court should note that consistent with its order, TWP has timely paid all post rehabilitation claims and will continue to do so. The $12 million estimated surplus from the proposed transaction will be added to TWP's other assets for the payment of claims under the liquidation.

VIII. The first amended rehabilitation plan does not force providers into non-negotiated relationships

Some of the creditors have expressed concern as to how provider relationships will be "handled on a going forward basis." They believe that they are being forced to continue to do business with Amerigroup without any recourse.

It is important to note that under the proposed transaction and court order the healthcare providers are not locked into a static contract. The proposed order fully anticipates that the providers will be able to renegotiate the terms of their relationship, including terms of payment, with Amerigroup before September 30, 2005.

The continuation of the provider contracts for 12 months after the assignment of the contracts to Amerigroup is essential to the success of the proposed transaction. By extending the contracts the Court will:

1. Assure that Amerigroup has a stable provider network so that it can bid for Medicaid contract.

2. Preclude Amerigroup form refusing to work was the providers to reach a mutually beneficial contract as quickly as possible.

3. Preclude the providers from extracting commercially unreasonable contract terms from Amerigroup. based on their ability to "kill the deal" if Amerigroup does not concede to their demands.

4. Places both Amerigroup and the providers an equal footing for contract negotiations give and them a reasonable period of time to reach mutually beneficial agreements.

The Court may note that the requested continuation for the contracts will bring the total amount of time that the contracts are continued under their existing terms to a maximum of 26 months. That is far shorter than the 72 months that Judge Giddings authorized the continuation of the OmniCare provider contracts in his approval of Omni cares first amended rehabilitation plan.

IX. Requiring medical providers to maintain their contracts with Amerigroup for up to 12 months does not unconstitutionally impair their contracts

Some providers claim, without citing authority, that an injunction preventing them from terminating their contracts with Amerigroup will impair their contractual rights in violation law. They also assert that there is no legal authority for the court to extend the contracts. The providers are wrong.

The test set forth in *Linton v Commissioner of Health and Environment, State of Tennessee*, 65 F.3d 508, 517 (6th Cir 1995) provides a legal standard to determine whether or not contract rights have been impermissibly impaired by state action. As stated by the *Linton* court, the test is:

1. Is there a substantial impairment of a contract right?

2. If so, is there a "significant and legitimate public purpose behind the regulation alleged to impair the contract. . ."; and,

3. If there is, is the adjustment of rights and responsibilities based on reasonable conditions and appropriate for the public purpose of the legislation? *Id.*

In analyzing the proposed contract extension, it is important to note:

1. Laws that exist when a contract made are part of the contract as if they were expressly referred to and incorporated by its terms. *Nichols v State Administrative Board*, 338 Mich 617, 622 (1954).

2. "The primary determination of public need and character of remedy in the exercise of the police power is in the Legislature. Unless the remedy is so palpably unreasonable and arbitrary so as to needlessly invade property or personal rights as protected by the Constitution, the act must be sustained. The presumption favors validity and, if the relation between the statute and the public welfare is debatable, the legislative judgment must be accepted." *Carolene Products Co v Thomson*, 276 Mich 172, 178 (1936).

3. "Undeniably, health is a matter of state concern . . . in safeguarding the public health, the Legislature is granted a large area of discretion as to the measures to be used, it being no longer questioned that the State may interfere directly or indirectly by any of its agencies whenever public interest demands it." *City of Ecorse v Peoples Community Hospital Authority*, 336 Mich 490, 501 (1953).

4. "[T]he reservation of the reasonable exercise of the protective power of the State is read into all contracts . . . ." *Home Building and Loan Association v Blaisdell*, 290 US 398, 444; 54 S Ct 231, 242; 78 L Ed 413, 432 (1934).

5. Delaying the right to enforce a contractual remedy will not unconstitutionally impair the contract, if reasonable compensation is provided. *Joint Stock Land Bank of Charleston v Hudson*, 266 Mich 644, 646-650 (1934).

6. The State, through the exercise of its police powers, may prevent the immediate and literal enforcement of contractual obligations by a temporary and conditional restraint, where

vital public interests would otherwise suffer . . . ." *Home Building and Loan Association v Blaisdell*, 290 US 398, 440; 54 S Ct 231, 241; 78 L Ed 413, 430 (1934).

7. The right to terminate a contractual relationship may be limited without unconstitutionally impairing the contract. *See*, *Block v Hirsh*, 256 US 135; 41 S Ct 458; 65 L Ed 865 (1921) [Court upheld use of police power to preclude landlords from terminating leases.]

A. Maintaining TWP's provider network does not impair the providers' contract rights

Factually, there can be no impairment of providers' contractual rights by the Commissioner's exercise of the authority granted by MCL 500.8101 *et seq.* *Linton*, 65 F.3d at 517. The providers' contracts cannot be impaired by a statue that was in force when the contract was made. *Oshkosh Water Works Co. v City of Oshkosh*, 187 US 437, 446; 23 S Ct 234, 237; 47 L Ed 249, 253 (1902). In fact, in *Mendel v Gardner*, 283 Ark 473, 476, 678 SW2d 759, 761 (1984), the court stated:

> The rehabilitation of insurance companies pursuant to state insolvency laws does not impair the obligation or contracts. *Neblett v Carpenter,* 305 US 297 (1983); *Lewelling v Manufacturing Woodworkers Underwriters,* 140 Ark 124, 215 SW 258 (1919).

Even if the Court's injunction could impair the providers' contract, the impairment would not be substantial. Providers are merely required to maintain their contractual relationships with TWP's assignee. They will provide medical services just like they did before rehabilitation. They will operate under the same contract they did before rehabilitation and they will receive compensation at the same rates as they did before rehabilitation. The only difference is, that because of the rehabilitation and the proposed transaction the providers and other creditors have a much better chance of receiving full payment of their pre and post-rehabilitation claims. Thus, contrary to the providers' assertion, there is no impairment of their reasonable expectations under their contracts. The proposed transaction and proposed court order will allow the providers to

negotiate a mutually beneficial agreement with Amerigroup or if after reasonable period of time they cannot reach an acceptable agreement with Amerigroup, the providers can terminate their contracts. These provisions provide sufficient safeguards to prevent a substantial impairment of the providers' contractual rights.

In addition, health care providers are engaged in a highly regulated industry. The same is true of the insurance companies that pay for their services. Thus, providers entered into their contracts with TWP knowing that both parties were subject to the State's regulation of their relationship. One of the known risks was that the Commissioner could place TWP into rehabilitation. MCL 500.3503 and MCL 500.8101(3)(f). Providers were also aware that if TWP was placed into rehabilitation, the Commissioner is statutorily authorized to:

- Continue the operation of TWP as part of a rehabilitation proceeding MCL 500.8112 and MCL 500.8114(2)
- Take such action she considers necessary and appropriate to accomplish the rehabilitation MCL 500.8114(2).
- Receive from the Court a restraining order, permanent injunction, and any other order considered necessary and proper to prevent:

  "[T]hreatened or contemplated action that might lessen the value of TWP's assets or prejudice the rights of its members, it creditors, shareholders, or the administration of the rehabilitation." MCL 500.8105(1).

Accordingly, providers cannot complain that the Rehabilitator has exercised her statutory authority to regulate their contractual relationship with TWP and its assignee.

Based on the facts of this case the providers' allegations of unconstitutional impairment of their contractual rights does not pass the first hurdle of the *Linton* test.

B. Even a substantial impairment of DMC's contract rights would not be a constitutional violation

Even if the providers could prove a substantial impairment of their contract rights, there is still no constitutional violation. The State has a legitimate and significant interest in:

- Ensuring that there are sufficient financially sound HMOs to spread the risks associated with providing cost effective health care to Medicaid and commercial consumers.
- "Regulat[ing] the health delivery aspects of health maintenance organization operations for the purpose of assuring that health maintenance organizations are capable of providing care and services promptly, appropriately, and in a manner that assures continuity and acceptable quality of care." MCL 500.3513(1); and
- "[A]ssuring that HMOs operate in the interest of enrollees consistent with overall health care cost containment while delivering acceptable quality of care and services that are available and accessible to enrollees with appropriate administrative costs and health care provider incentives." MCL 500.3513(2).
- Protecting HMO members and the general public from risks associated with the uncontrolled withdrawal of providers from an HMO's provider network.
- Regulation of HMOs and their insolvency.

Since the State has a significant and legitimate public purpose for the orderly transition of TWP, the providers must show that the adjustments to their contractual rights are unreasonable and inappropriate to address the State's concerns. In this regard, the providers must admit that if they and TWP's other creditors are going to benefit from the proposed transaction, TWP's provider network must be maintained. The failure to do so would result in the frustration of the State's legitimate public interests and the loss of millions of dollars for the creditors.

The method used to maintain the provider network is an injunction that:

- Requires providers to maintain their relationship with TWP's assignee by continuing to provide medical services to its members under the terms of their pre-rehabilitation contracts.
- Requires TWP's assignee to pay for the medical services at the pre-rehabilitation contract rates.
- Provides for the amendment of the terms and conditions of the relationship, including the payment rates;
- Allows the judicial review of the relationship;
- Allows for judicial termination of the relationship when appropriate.

These provisions provide ample protection for the providers' interests and contractual expectations. They accomplish the State's objectives without significantly altering the providers' contractual rights. Thus, the Court's order is reasonably related to the protection of the State's interests. Accordingly, the Court's order does not unconstitutionally impair the providers' contract rights. Therefore, the providers' objections to the legality of the proposed transaction should be dismissed.

X. The sale of TWP's HMO license to Amerigroup is authorized by the Insurance Code

The Rehabilitator has previously demonstrated that as a losing bidder, Molina Health Care of Michigan (Molina) has no standing to object to the Rehabilitator's petition for approval of the proposed sale. (See part III supra, pages 14 to 19.) Therefore Molina's objections should be disregarded entirely.

In any event, Molina's objection to the transfer of TWP's certificate of authority is wrong. Molina claims that the sale of TWP's license is unlawful because no provision in the

Insurance Code allows the transfer of an HMO license to another entity. Molina objection pp 3-4, § B. Molina premises its argument on MCL 500.435(3) which provides:

> A certificate of authority at all times remains the property of the State. Upon termination at the request of the insurer or revocation by the Commissioner, the certificate of authority shall be delivered promptly by the insurer to the Commissioner.

Molina's argument is misplaced. The Insurance Code explicitly contemplates the control of an HMO may be obtained by means other than a merger. Under Chapter 81 the Rehabilitator is explicitly authorized to "[T]ake such action as he or she considers necessary or appropriate to reform and revitalize the insurer...." MCL 500.8114(2). One form of revitalization is to transfer control of an insurer's certificate of authority (license) to an insurer that has the experience, financial stability, and resources to effectively operate an HMO consistent with the requirements of Michigan law. The mechanism provided for this type of transfer of control of a certificate of authority is set forth in MCL 500.1311 and MCL 500.1315.

Consistent with requirements of MCL 500.1311 and MCL 500.1315, Amerigroup has made a preliminary Form A filing with the Rehabilitator and is in the process of completing all Form A requirements for submission. Preliminary indications are that approval should be forthcoming. Form A is a statement regarding the acquisition of control of a domestic insurer pursuant to MCL 500.1311. Form A requires information in the following areas: (1) method of acquisition, (2) identity and background of the applicant, and (3) individuals associated with the applicant, (4) the nature, source and amount of consideration, (5) future plans for the insurer, (6) recent recommendations to purchase, (7) financial statements and exhibits. Hence, approval by the Commissioner as the state regulator will be required in order for Amerigroup to act as a health maintenance organization. MCL 500.1311 permits domestic insurers to be purchased. Traditionally, under Form A, license is transferred to the new owner when purchasing a

corporate entity and the Commissioner approves the transaction. It is not an unusual industry practice of insurance that the business and liabilities are transferred out of a corporate entity so that the corporate entity is a shell, and that shell, including its license, are then purchased. The fact that the corporation will be liquidated does not affect the ability of the certificate of authority to be transferred. Sale of the license can be done in receivership proceedings because the license is an asset and part of the receivership estate, which is overseen by the Court. The Commissioner is given extremely broad powers under chapter 81 to reorganize and restructure entities in rehabilitation. The rehabilitator's job is to marshal and maximize the insurer's assets. In this case the sale of the TWP license will bring a great amount of money into the estate to pay creditors. Consequently, this Court's approval of the sale does not negate the necessity for seeking approval of the purchase by filing a Form A with the Commissioner. During the Form A review the above-referenced areas will be reviewed by the Commissioner to assure that the new buyer will be able to operate the health plan successfully. Consequently, the Court's approval of the sale remains subject to change in control approval by the OFIS Commissioner.

XI. The Michigan State Medical Society has no standing to object to the proposed sale of assets

The Michigan State Medical Society (MSMS) is not a creditor of TWP. Although it purports to represent over 14,000 physicians, it does not allege or assert that it is pursuing its objection on their behalf. In fact, most of its members are not creditors of TWP.

MSMS asserts that **its** objections are supported by Drs. Andaya and Michael. The Court may note, however, that neither Dr. Andaya nor Dr. Michael have filed individual objections to the proposed sale of assets.

Standing to assert an objection to the proposed transaction is limited to claimants, creditors, the public, and policyholders that will be affected by the rehabilitation plan. See MCL

500.8101(3). MSMS is not a real party in interest to this litigation. It has no interest in the approval or disapproval of the proposed sale of assets or the payment of creditor claims. Since it is not a real party in interest to the rehabilitation plan, the rehabilitation proceedings or TWP's contract with the Department of Community Health, it has no basis to assert objections to the proposed transaction. MCL 2.201(B). See also, *Michigan National Bank v Mudgett*, 178 Mich App 677, 679 (1989).

MSMS's assertion of standing pursuant to MCL 500.8101(3) as a member of the public is without merit. MSMS does not purport to represent the interests of the public. MSMS represents only physicians, most of which are not TWP providers and who will not be impacted by the sale of TWP's assets. Furthermore, of the MSMS members who are TWP providers, none have filed objections to the proposed transaction.

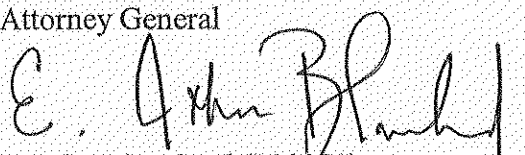
Based on the foregoing, Linda A. Watters, Commissioner of the Office of Financial and Insurance Services, and Rehabilitator of TWP, requests that this Court dismiss the MSMS's objections to the proposed sale.

RELIEF

WHEREFORE, the Rehabilitator respectfully requests that the Petition for Approval of the Rehabilitator's Plan to Sell Assets of The Wellness Plan to Amerigroup Michigan, Inc. be approved.

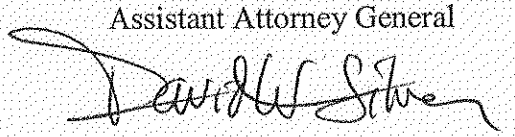
Respectfully submitted

Michael A. Cox
Attorney General

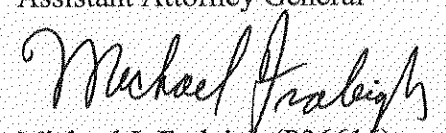


E. John Blanchard (P28881)
Assistant Attorney General

William A. Chenoweth (P27622)
Assistant Attorney General



David W. Silver (P24781)
Assistant Attorney General



Michael J. Fraleigh (P36615)
Assistant Attorney General

Insurance & Banking Division
P.O. Box 30754
Lansing, Michigan 48909
(517) 373-1160

Dated: April 23, 2004

STATE OF MICHIGAN
CIRCUIT COURT FOR THE 30TH JUDICIAL DISTRICT
INGHAM COUNTY

LINDA A. WATTERS, COMMISSIONER,
OFFICE OF FINANCIAL AND INSURANCE SERVICES
FOR THE STATE OF MICHIGAN,

Petitioner,

Case No. 03-1127-CR

v

Hon. William E. Collette

THE WELLNESS PLAN,
a Michigan Health Maintenance Organization,

Respondent.
_____/

AFFIDAVIT OF JUDITH A. WEAVER

State of Michigan)
) ss
County of Ingham)

JUDITH A. WEAVER, being first duly sworn, deposes and says that:

1. She is a Deputy Commissioner of the Office of Financial and Insurance Services, and is in charge of the Supervisory Affairs & Insurance Monitoring Division.

2. She has been employed by the Office of Financial and Insurance Services for approximately 20 years.

3. Her responsibilities include: monitor the financial condition of insurance entities licensed to do business in Michigan; recommend appropriate regulatory action to the Commissioner when necessary; oversee the receivership unit; oversee consultants hired as part of the receivership proceeding, including Deputy Rehabilitators, and act as directed by the Rehabilitator; oversee the financial review of applications for licensure and make

ATTACHMENT 1

recommendations; and oversee review of applications for approval for change of control and make recommendations.

4. She is familiar with The Wellness Plan, including its financial condition, and its rehabilitation before this Court.

5. She has assisted the Rehabilitator by reviewing financial reports submitted by The Wellness Plan, including the annual financial statement for the period ending December 31, 2003. In the annual filing, The Wellness Plan reported capital and surplus of $8,606,172 and a risk-based capital level of 122%. In order to meet the risk-based capital requirement as required in MCL 500.3551(4), The Wellness Plan would need a risk-based capital level of 200%. The Wellness Plan needed a capital and surplus level above $14,110,542. The Wellness Plan's capital and surplus level was deficient by $5,504,370. The Wellness Plan's risk-based capital level at December 31, 2003 was in the regulatory action level as defined in Insurance Bulletin 98-02.

6. As part of the annual filing, The Wellness Plan filed form FIS 0321 entitled Working Capital Calculation. On this form, The Wellness Plan reported its working capital was a negative $29,442,089. MCL 500.3555 provides that a health maintenance organization shall maintain a financial plan evaluating, at a minimum, cash flow needs and adequacy of working capital. A health maintenance organization must provide for adequate working capital, which shall not be negative at any time.

7. She has assisted the Rehabilitator by working with the Deputy Rehabilitators in the management of The Wellness Plan, engaging in communication with potential buyers, participating in discussions with potential buyers, participating in the Rehabilitator's request for

bid process, overseeing the due diligence process, and participating with the Rehabilitator in the process to review, analyze and evaluate the bid submissions.

8. She has read the Rehabilitator's Response to the Objections to the Petition for Approval of the Rehabilitator's Plan to Sell Assets of The Wellness Plan to Amerigroup Michigan, Inc., and to the best of her knowledge and belief, the factual allegations set forth in the Response concerning the financial reporting information, and the request for bid and selection process is true and correct.

Judith A. Weaver
JUDITH A. WEAVER

Subscribed and sworn to before me
this 23rd day of April, 2004.

Stephanie Andreadis
STEPHANIE ANDREADIS
Notary Public, Eaton County, MI
(Acting in Ingham County)
My Commission Expires: 11/21/07